



MARYLAND HEALTH CARE COMMISSION

4160 PATTERSON AVENUE – BALTIMORE, MARYLAND 21215
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MEMORANDUM

To: Commissioners

From: Kevin R. McDonald, Chief
Certificate of Need

Date: July 10, 2014

Re: Staff Report and Recommendation:
Request to Modify a Certificate of Need
College View Center
Docket No. 12-10-2336

Attached is a Staff Report and Recommendation in the review of the request for a modification of a Certificate of Need ("CON") issued on December 20, 2012 to College View Center ("College View"). Operated by Genesis HealthCare ("Genesis") and owned by Health Care REIT, the project would construct a 130-bed replacement comprehensive care facility about 2.3 miles from its current location at 700 Toll House Avenue to a location on Ballenger Drive in Frederick County. The replacement facility would include the 119 beds from the existing facility and 11 beds acquired from Frederick Memorial Hospital, which formerly operated the beds as an in-hospital CCF unit.

College View requests authorization to increase total project costs by approximately \$1.35 million, bring the total to \$20,466,811. The applicant identified the following reasons for the project cost increase: construction bids exceeded pre-bid construction cost estimates by approximately \$491,000; site preparation costs increased by \$286,500; and equipment cost increased by about \$128,000. In addition, capitalized construction interest costs are now estimated to be almost \$1.05 million above the original estimate of \$990,000; the applicant attributed this increase to project delays caused by the need for additional surveys, more extensive site preparation, and other engineering issues. With these increases, the total anticipated cost increase is \$1,351,589 (about 7.1%), which exceeds the permissible inflation allowance

Staff recommends that the Commission **APPROVE** the proposed modification of the Certificate of Need issued to College View Center to construct a 130-bed replacement

comprehensive care facility (Docket No. 12-10-2336), with the same standard condition issued with the 2012 CON, which is:

At the time of first use review, the College View Center operator shall provide the Commission with a completed Memorandum of Understanding with the Maryland Medical Assistance Program agreeing to maintain the proportion of Medicaid patient days required by Nursing Home Standard COMAR 10.24.08.05A(2).

IN THE MATTER OF
COLLEGE VIEW CENTER
DOCKET NO.12-10-2336

* BEFORE THE
*
* MARYLAND HEALTH
*
* CARE COMMISSION
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REQUEST TO MODIFY CERTIFICATE OF NEED

I. INTRODUCTION

The Maryland Health Care Commission (“Commission or MHCC”) granted College View Center (“College View”), operated by Genesis HealthCare (“Genesis”) and owned by Health Care REIT, a Certificate of Need (“CON”) to construct a 130-bed replacement comprehensive care facility (“CCF”) on December 20, 2012. The replacement facility was approved for a location on Ballenger Drive in Frederick County, about 2.3 miles from its current location at 700 Toll House Avenue. The replacement facility incorporated 119 beds from the existing facility and 11 beds acquired from Frederick Memorial Hospital, which had formerly operated the beds as an in-hospital CCF unit. MHCC awarded this CON with an approved project cost of \$19,115,222 and with the following standard condition:

At the time of first use review, the College View Center operator shall provide the Commission with a completed Memorandum of Understanding with the Maryland Medical Assistance Program agreeing to maintain the proportion of Medicaid patient days required by Nursing Home Standard COMAR 10.24.08.05A(2).

College View has requested authorization to increase the total project costs by approximately \$1.35 million, bringing the total project costs to \$20,466,811. The applicant identified the following reasons for the project cost increase: construction bids exceeded pre-bid construction cost estimates by approximately \$491,000; site preparation costs increased by \$286,500; and equipment costs increased by about \$128,000. In addition, capitalized construction interest costs are now estimated to be almost \$1.05 million above the original estimate of \$990,000. The applicant attributed this increase to project delays caused by the need for additional surveys, more extensive site preparation, and other engineering issues. With these increases, the total anticipated cost increase is \$1,351,589 (about 7.1%), which exceeds the permissible inflation allowance.

The replacement facility is under construction, which was initiated in 2013 with an expectation that the project could be completed within the allowable increase in approved project cost. This request was filed because that expectation could not be realized.

II. APPLICABLE REGULATIONS

Under the Commission’s regulations, at COMAR 10.24.01.17B, the following changes to an approved CON require the Commission’s approval:

1. A significant change in physical plant design;
2. Capital Cost increases that exceed the approved capital cost inflated by an amount determined by applying the Building Cost Index published in Healthcare Cost Review from the application submission date to the date of the filing of a request for approval of a project change;
3. When total projected operating expenses or revenue increases exceed the projected expenses or revenues in the approved Certificate of Need Application, inflated by 10 percent per year;
4. Changing the financing mechanisms of the project; or
5. Changing the location or address of the project.

College View Center's request to modify its CON for this project involves a capital cost increase that exceeds the approved capital cost inflated by an amount determined by applying the Building Cost Indices published in Healthcare Cost Review (COMAR 10.24.01.17B(2)) from the date that College View initially submitted its CON application (July 6, 2012) to the date it filed the request for approval of the project change (June 4, 2014).¹ Accordingly, this request must be reviewed and approved by the Commission.

The actions available to the Commission are found in **COMAR 10.24.01.17D(3)**:

- (3) The Commission shall provide written notification to the applicant within 45 days of the Commission's receipt of the change request that:
 - (a) The proposed change is approved and is incorporated into a modified Certificate of Need for the project;
 - (b) The proposed change is approved in part or approved with conditions;
 - (c) The proposed change is not approved, with explanation; or
 - (d) The proposed change is of sufficient scope to warrant complete review in accordance with the Certificate of Need review process described in Regulations .08—.10 of this chapter, and may only be considered upon completion of this review.

III. COST INCREASES AND FINANCIAL IMPACT OF THE PROPOSED MODIFICATION

CON-approved cost compared to modification request

Table 1 compares the project cost estimate as originally approved by the Commission to the estimated costs in the modification request submitted by College View.

¹ College View's request to modify the CON does not involve any significant change in physical plant design, an increase in operating expense or revenue, or a change in either financing or location of the project.

Table 1: Comparison of Approved Project Cost and New Cost Estimate

Project Elements	Original Approved Amount	Requested Modification	Change	% change
Capital costs				
Building	\$9,930,000	\$10,420,928	\$490,928	4.9%
Land Purchase	2,520,000	2,520,000	0	0.0%
Site Preparation	1,050,000	1,336,500	286,500	27.3%
Architect/ Engineering Fees	350,000	350,000	0	0.0%
Permits	100,000	100,000	0	0.0%
Major and Minor Movable Equipment	1,420,000	1,548,092	128,092	9.0%
Contingencies	450,000	227,459	-222,541	-49.5%
Other (Performance Bonds)	150,000	146,718	-3,282	-2.2%
Inspections-Bank	20,000	20,000	0	0.0%
Survey	10,000	10,000	0	0.0%
Appraisal & Feasibility	60,000	60,000	0	0.0%
Developer Fees	700,000	700,000	0	0.0%
Total Current Capital Costs	\$16,760,000	\$17,439,697	\$679,697	4.1%
Non-current Capital Costs				
Interest (Gross)	\$990,000	\$2,037,512	\$1,047,512	105.8%
Inflation	460,222	84,602	-375,620	-81.6%
TOTAL PROPOSED CAPITAL COSTS	\$18,210,222	\$19,561,811	\$1,351,589	7.4%
Loan Placement Fees	190,000	190,000	0	0.0%
Legal Fees (CON related)	40,000	40,000	0	0.0%
Legal Fees (Other)	150,000	150,000	0	0.0%
Consultant Fees (CON application assistance)	25,000	25,000	0	0.0%
Working Capital Startup Costs	500,000	500,000	0	0.0%
TOTAL PROJECT COST	\$19,115,222	\$20,466,811	\$1,351,589	7.1%

The following is a summary of College View's explanation of the increases to the project cost estimate:

- **Construction costs:** Bids came in higher than expected and change orders have also been made during construction. In combination, this has increased construction cost by \$490,928 (about 4.9% over approved costs).
- **Site preparation:** A second site survey performed after the CON application cost estimate identified issues that required a greater degree of engineering and fill than initially anticipated, increasing the cost for preparing the site by \$286,500 (27.3%).
- **Equipment:** The cost of movable equipment increased from \$1.42 million to \$1,548,092, a difference of \$128,092 (9.0%). Most of this cost increase is attributed to price inflation over the past two years. Additionally, the budget for information technology equipment was increased due to advancement in IT system capabilities viewed as necessary by the applicant.

- **Interest:** The estimate of capitalized construction interest has increased from \$990,000 to \$2,037,512 (105.8%). This increase in interest expenses during the construction period is due to project delays caused by the need for additional surveys and more extensive site preparation and other engineering work..

\$222,541 in contingency cost allocation offset some of the increase in project costs.

The source of funds for the additional project costs is cash reserves from Genesis.

Inflation allowance

Capital cost increases that exceed the inflation allowance calculated using the building cost indices published on a quarterly basis by IHS Global Insight in Healthcare Cost Review require Commission approval under COMAR 10.24.01.17B(2).

Inflation is figured from the CON application's submission date (July 6, 2012 or the 3rd quarter of CY 2012) to the date of the filing of a request for CON modification (June 4, 2014 – or the 2nd quarter of CY 2014). The allowable inflated capital cost is **\$18,210,222²**, with an allowable inflation level of **\$460,222** over the originally-approved capital cost. The projected cost increase of **\$1,351,589** exceeds the allowable inflation level and, therefore, requires the Commission's review and approval.

Impact on operating cost and revenue

College View indicated in the December 2012 CON approval that the proposed facility would reach profitability by the third full year of operation after project completion. The revised revenue and expense statement indicates that College View continues to project profitability (net revenue in excess of operating expenses) by the third full year of operation. Based on a 40-year depreciation schedule, the impact of the project cost increase is estimated by Genesis to be \$36,670 per year over the life of the asset. Genesis projects that 84% of patient days will be paid for by Medicare or Medicaid reimbursement rather than prices charged by the facility.

IV. ANALYSIS AND RECOMMENDATION

The Commission's regulations identify certain circumstances where a modification is not permissible and the applicant requires a new Certificate of Need. COMAR 10.24.01.17C states:

1. Changes in the fundamental nature of a facility or the services to be provided in the facility from those that were approved by the Commission;
2. Increases in the total licensed bed capacity of medical service categories from those approved;
3. Any change that requires an extension of time to meet the applicable performance requirements specified under Regulation .12 of this chapter, except as permitted under Regulation .12E of this chapter.

² Using the Building Cost Indexes reported in the MHCC's June 18, 2014 edition of the "Increase in the Cost of Approved Project Requiring Commission Approval."

The modification will not change the fundamental nature of the project or the services provided by this replacement; the total number of beds will remain the same as previously approved; and the applicant has not requested or will not need an extension of time to meet the applicable performance requirements. Therefore, the modification requested by College View is permissible under paragraph .17C.

Although the increase in the total project cost is significant (about 7.1%), the proposed modification will not have a material effect on the findings made by the Commission on December 20, 2012 with respect to the cost and effectiveness of alternatives or project viability. Because there are no material changes occurring either in the location, capacity, or nature of the project, the requested modification does not change the need for the project or its impact on existing providers.

The modification by College View does not propose additional nursing home beds that will serve Frederick County. The proposed facility will replace an existing CCF with a larger and more modern facility.

The additional costs for completion of this project will not have a material adverse impact on the financial viability of the facility, on Genesis HealthCare, one of the largest operators of nursing homes in the country, or on the owner of the real assets, the publically-traded Health Care REIT, which had a market capitalization of \$17.3 billion in May, 2014. . Financial and non-financial resources necessary to implement and sustain the project are available.

Staff recommends that the Commission **APPROVE** the proposed modification of the Certificate of Need issued to College View Center to construct a 130-bed replacement comprehensive care facility (Docket No. 12-10-2336), maintain the same condition attached to the 2012 CON, which is:

At the time of first use review, the College View Center operator shall provide the Commission with a completed Memorandum of Understanding with the Maryland Medical Assistance Program agreeing to maintain the proportion of Medicaid patient days required by Nursing Home Standard COMAR 10.24.08.05A(2).

IN THE MATTER OF	*	BEFORE THE
	*	
COLLEGE VIEW CENTER	*	MARYLAND HEALTH
	*	
DOCKET NO. 12-10-2336	*	CARE COMMISSION
	*	

FINAL ORDER

Based on Commission Staff's analysis and findings, it is this 17th day of July, 2014,
ORDERED that:

The request for modification of a Certificate of Need submitted by 700 Toll House Avenue Operations, LLC, d/b/a College View Center, to relocate and build a 130-bed replacement comprehensive care facility on Ballenger Drive in Frederick County, Docket No. 12-10-2336, at an estimated cost of \$20,466,811, be **APPROVED**, subject to the following condition:

At the time of first use review, the College View Center operator shall provide the Commission with a completed Memorandum of Understanding with the Maryland Medical Assistance Program agreeing to maintain the proportion of Medicaid patient days required by Nursing Home Standard COMAR 10.24.08.05A(2).

MARYLAND HEALTH CARE COMMISSION
 July 17, 2014